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Central Intelligence Agency

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DIRECTORATE OF INTELLIGENCE

18 June 1985

Czechoslovakia: An Economic Overview

Summary

Czechoslovakia this year has continued the slow economic growth it registered in the previous two years. Real living standards, however, languish at the level of the late 1970s, and the leadership has yet to take action to address the serious problems facing the economy including the rapidly aging industrial base, the enormous waste of energy and raw material inputs, and the poor competitiveness of exports. There appears to be little movement toward policy initiatives among the stand-pat leadership and, without a change in leadership personnel or a push from Moscow, the economy probably will be unable to generate much growth in coming years. Indeed, any unfavorable external development--such as an economic downturn in the West or sharply increased Soviet economic demands--could bring economic growth to a halt.

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Domestic Economy

Based on western national income accounting methods, GNP grew by about two percent in 1983 and 1984 and should show similar results this year. Record grain harvests--resulting from good weather rather than good policy--and some economic recovery in the West helped move the economy out of stagnation. Czechoslovak statistics, meanwhile, showed a strong rebound in national income and industrial production, but these strong gains would be substantially reduced by taking account of depreciation, particularly in the industrial sector. 25X1

Despite its disappointment with economic performance, the insecure leadership has been unwilling to overhaul the economy's rigid central planning mechanisms. A half hearted economic reform introduced in 1981, the "Set of Measures", has had little impact because of its limited scope and because of subsequent backtracking by the regime. The decision to cut investment and machinery imports from the West in order to improve the hard currency payments picture has resulted in an increasingly aging industrial base. Leadership attempts to bolster productivity and efficiency by exhortation and calls for increased discipline at the work place have yielded little return. 25X1

The government recognizes the critical need for modernization of plant and equipment but has so far done little because of other claims on investment resources and its conservative policies toward foreign debt. Plans to increase substantially expenditures on electronics, computers and new plants and machinery have been blocked by the need to allocate about half of total investment to mining, power plants, and energy equipment. Rigidities in the economy and poor planning have led, in particular, to delays and cost overruns in nuclear power plant construction, leaving few investment resources for other projects. A related problem facing the economy is the increasing stockpiles of goods that are unsalable on the domestic market due to poor quality. The Czechoslovak press also reports that intermediate products are taking longer to reach the next stage in the production process because of bottlenecks and inefficiency. 25X1

As a result of economic stagnation, living standards probably are lower now than they were five years ago. The regime, unable to provide the population with the improvements in living standards that they enjoyed in the 1970s, faces deep--and apparently growing--popular alienation. Discontent is expressed not in unrest or open defiance but in passive resignation, cynicism, and escapism. Employees at all levels leave work to take care of private errands; workers often moonlight on company time and with company materials; and absenteeism, alcoholism, and corruption are rampant. 25X1

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Foreign Trade, Debt, and Finance

In external economic relations, the regime has chosen the path of greater integration with other CEMA countries and an elimination of the hard currency debt in order to reduce dependence on the west. This policy has succeeded in reducing the already small debt to about $2 billion at year-end 1984; and the socialist countries' share of total Czechoslovak trade has jumped to about 80 percent in 1984, compared with 70 percent in 1980. In our view, however, CEMA countries will be unable to provide Prague with the sophisticated equipment needed to modernize the economy and restore sustainable economic growth. The USSR, moreover, is demanding better quality goods and more investment in Soviet projects from its CEMA partners, which will represent a further burden for the Czechoslovak economy. 25X1

Czechoslovakia's cutbacks in imports from the West have enabled it to run a $800 million trade surplus with the non-socialist countries in 1984--its largest ever--and a $200 million surplus with the developed west--the first in almost twenty years. Trade with LDCs accounts for most of Czechoslovakia's surplus, with arms, machinery and transport equipment, and turnkey plants the most important exports. However, the Czechoslovaks have reported problems collecting debts from some developing countries. 25X1

Nonetheless, the financial press occasionally reports that Prague is interested in raising new credits from Western banks. Moreover, some economic officials have indicated the country will eventually resume modest borrowing to finance needed Western imports. With the low level of debt and strong payments performance, Western banks seem willing to lend to Prague on very favorable terms. Czechoslovak banking and financial officials may be able to convince the leadership that the time has come to ease the prohibition on foreign borrowing if only to maintain the country's presence in the international loan market. While Prague may decide to raise a loan, it is unlikely to launch a major borrowing campaign. 25X1

Czechoslovakia continues to run large deficits with the Soviet Union--453 million rubles in 1984, compared to 519 million rubles in 1983. Prague appears to be facing increased pressure to reduce these deficits and to provide more and better quality goods to the USSR. The Czechoslovaks also have agreed to step up participation in Soviet development projects, especially in energy, to ensure the maintenance of Soviet deliveries of energy and raw materials. Projects include the Progress gas pipeline, the Krivoy Rog iron ore extraction plant, and assistance in building the new gas pipeline to Western Europe. 25X1

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Outlook

Near-term prospects are bleak for sustainable economic growth. The present stasis in Czechoslovak decisionmaking is likely to remain until broken by the removal of Husak from the scene, a major change in Soviet guidance, or a sharp downturn in economic performance. Prague is doubtless closely watching developments in Moscow since Gorbachev's accession to see if a major tack in policy direction is warranted. For example, if Gorbachev embarks on--or even signals--major economic reform, Prague probably will quickly follow suit. A sharp economic decline probably also would compel the Czechoslovak leadership to adopt a more liberal approach toward foreign borrowing or to accept the uncertainty and risks that accompany economic reform. Finally, Husak's departure from the scene--for either health reasons or a push from Moscow--could precipitate major, and long overdue, personnel changes and could shift the balance in the leadership toward those who favor new policies. 25X1

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